



FEDERAL RESERVE SYSTEM

12 CFR Part 210

[Regulation J; Docket No. R- 1599]

RIN 7100-AE98

Collection of Checks and Other Items by Federal Reserve Banks and Funds Transfers Through Fedwire

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: The Board of Governors of the Federal Reserve System (Board) is publishing final amendments to Regulation J. The amendments clarify and simplify certain provisions Regulation J, remove obsolete provisions, and align the rights and obligations of sending banks, paying banks, and Federal Reserve Banks (Reserve Banks) with the Board's recent amendments to Regulation CC to reflect the virtually all-electronic check collection and return environment. The final rule also amends Regulation J to clarify that terms used in financial messaging standards, such as ISO 20022, do not confer legal status or responsibilities.

DATES: Effective January 1, 2019.

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SUPPLEMENTARY INFORMATION:

I. Background

Subpart A of Regulation J governs the collection of checks and other items by the Reserve Banks. This subpart includes the warranties and indemnities that are given to the Reserve Banks by parties that send items to the Reserve Banks for collection and return, as well as the warranties and indemnities for which the Reserve Banks are responsible in connection with the items they handle. Subpart A also describes the methods by which the Reserve Banks may recover for losses associated with their collection of items. Subpart A authorizes the Reserve Banks to issue operating circulars governing the details of the collection of checks and other items and provides that such operating circulars have binding effect on all parties interested in an item handled by a Reserve Bank. The Reserve Banks' Operating Circular No. 3, "Collection of Cash Items and Returned Checks" (OC 3),¹ is the operating circular that is most relevant to the Reserve Banks' check collection activities. Subpart B of Regulation J provides rules to govern funds transfers through the Reserve Banks' Fedwire Funds Service. This service is also governed by the Reserve Banks' Operating Circular No. 6, "Funds Transfers through the Fedwire Funds Service" (OC 6).²

II. Overview of Proposal and Comments

In March 2018, the Board published a notice of proposed rulemaking ("proposal") intended to align subpart A of Regulation J with the Board's 2017 amendments to Regulation CC and cross reference certain provisions (83 FR 11431). The proposal also included

¹ See, <https://www.frb services.org/assets/resources/rules-regulations/072315-operating-circular-3.pdf>.

² See, <https://www.frb services.org/assets/resources/rules-regulations/operating-circular-6-102917.pdf>.

amendments to subpart B of Regulation J to clarify that terms used in financial messaging standards, such as ISO 20022, do not confer legal status or responsibilities. The Board received 25 comments in response to its proposal during the comment period from a variety of commenters, including financial institutions, trade associations, clearinghouses, and private individuals. The Board has considered all comments received and has adopted amendments to Regulation J as described below.

A. Alignment with Regulation CC Amendments Addressing Electronic Checks

Under subpart A of Regulation J, Reserve Banks handle “items,” which are defined to include “electronic items.” Regulation J currently defines an “electronic item” as an electronic image of, and information describing, an item that a Reserve Bank agrees to handle pursuant to an operating circular. Regulation J also sets forth certain warranties provided to the Reserve Banks by the sender of an electronic item and certain warranties provided by the Reserve Banks when sending or presenting an electronic item. Specifically, Regulation J provides that for electronic items, the sender and the Reserve Banks make warranties (1) as set forth in the Uniform Commercial Code (U.C.C) and Regulation CC as if the electronic item were subject to their terms; and (2) similar to those made for substitute checks under the Check 21 Act (“Check-21-like warranties”). Regulation J also currently provides similar provisions related to checks that are returned as electronic items.

In 2017, the Board published a final rule amending Regulation CC to reflect the virtually all-electronic check collection and return environment (82 FR 27552). Among other things, the amendments created a regulatory framework for the collection and return of electronic items (i.e., electronic images and electronic information derived from a paper item) by defining the terms “electronic check” and “electronic returned check,” creating Check-21-

like warranties for electronic checks and electronic returned checks, and applying existing paper-check warranties to electronic checks and electronic returned checks.

In its proposal, the Board proposed to remove the term “electronic item” from Regulation J and define “check” and “returned check” to include an electronic check and electronic returned check as defined in § 229.2 of Regulation CC. The proposal defined the term “item” to include an electronic check as defined in Regulation CC. The Board also proposed to eliminate duplicative provisions by removing the Check-21-like warranties currently provided under Regulation J by the sender and the Reserve Banks. Instead, the proposal provided that the sender of an item (including an electronic check) and the Reserve Banks would (as applicable and unless otherwise provided) make all the warranties and indemnities set forth in and subject to the terms of subparts C and D in Regulation CC. The Board proposed similar amendments to the provisions of Regulation J that currently address returning checks as electronic items.

Commenters generally supported aligning Regulation J with Regulation CC’s amendments regarding electronic checks. The Board received specific comments on cross referencing Regulation CC electronic check warranties and indemnities, which is discussed in detail in the relevant section-by-section analysis. The Board has revised proposed §§ 210.6(b)(3) and 210.12(e) to extend the warranties with respect to electronic checks and electronic returned checks provided by Reserve Banks to the same scope of recipients as in Regulation CC, as discussed in detail in the relevant section-by-section analyses.

B. Electronically Created Items

In the 2017 amendments to Regulation CC, the Board included certain indemnities with respect to electronically-created items (ECIs), which are check-like items created in

electronic form that never existed in paper form. ECIs can be difficult to distinguish from electronic images of paper checks. As a practical matter, a bank receiving an ECI often handles it as if it were derived from a paper check. However, because there was no original paper check corresponding to the ECI, the warranties, indemnities, and other provisions of Regulation CC would not apply to those items. As the Board explained in the 2017 Regulation CC amendments, the payee and the depository bank are in the best position to know whether an item is electronically created and to prevent the item from entering the check-collection system. Therefore, to protect banks that receive ECIs during the check collection process, the Board's Regulation CC amendments provided indemnities that ultimately shift liability for losses to the depository bank. These losses could arise because the ECI (1) is not derived from a paper check, (2) was unauthorized, or (3) was transferred or presented for payment more than once.³ As described above, the final rule cross references Regulation CC's warranties and indemnities in Regulation J, including Regulation CC's ECI indemnities.

In its proposal, the Board explained that although Regulation J does not explicitly address ECIs, the definition of item in Regulation J does not encompass ECIs and therefore

³ 12 CFR 229.34(g) provides that each bank that transfers or presents an electronically-created item and receives a settlement or other consideration for it shall indemnify, as set forth in § 229.34(i), each transferee bank, any subsequent collecting bank, the paying bank, and any subsequent returning bank against losses that result from the fact that (1) the electronic image or electronic information is not derived from a paper check; (2) the person on whose account the electronically-created item is drawn did not authorize the issuance of the item in the amount stated on the item or to the payee stated on the item (for purposes of paragraph (g)(2), "account" includes an account as defined in § 229.2(a) as well as a credit or other arrangement that allows a person to draw checks that are payable by, through, or at a bank); or (3) a person receives a transfer, presentment, or return of, or otherwise is charged for an electronically-created item such that the person is asked to make payment based on an item or check it has already paid.

Regulation J does not allow for the handling of ECIs by the Reserve Banks. Specifically, Regulation J defines an item, in part, as “an instrument or a promise or order to pay money, whether negotiable or not” that meets several other requirements.⁴ The terms “instrument,” “promise,” and “order” are defined under the U.C.C. as requiring a writing.⁵ Because they never existed in tangible form and therefore do not qualify as writings, ECIs are not “items” as defined in Regulation J.

To provide greater clarity that Regulation J does not allow for the handling of ECIs by the Reserve Banks, the Board proposed to amend the definition of “item” in subpart A of Regulation J to state explicitly that the term does not include an ECI as defined in Regulation CC. Furthermore, because Regulation J is intended to provide rules for the collection and return of items by the Reserve Banks, the Board proposed to allow the Reserve Banks to require senders to provide warranties and indemnities that only “items” and any “noncash items” the Reserve Banks have agreed to handle will be provided to the Reserve Banks. The Board’s proposal also permitted the Reserve Banks to provide a subsequent collecting bank and a paying bank the warranties and indemnities provided by the sender. The Board requested comment on possible implications that this clarification and change related to ECIs in Regulation J may have on financial institutions or the industry more broadly. The Board

⁴ 12 CFR 210.2(i).

⁵ Terms not otherwise defined in Regulation J or Regulation CC have the meanings set forth in the U.C.C. Under the U.C.C., “instrument” means a “negotiable instrument” which is defined in part as “unconditional promise or order to pay a fixed amount of money.” U.C.C. 3-104. “Promise” is defined as “a written undertaking to pay money signed by the person undertaking to pay.” U.C.C. 3-103. “Order” is defined as “a written instruction to pay money signed by the person giving the instruction.” U.C.C. 3-103. “Writing” and “written” are defined as including “printing, typewriting, or any other intentional reduction to tangible form.” U.C.C. 1-201.

also requested comment on whether, and to what extent, the Board should consider amending Regulation J as part of a future rulemaking to permit the Reserve Banks to accept ECIs.

Three commenters, including a Federal Reserve Bank and a comment letter submitted by a group of trade associations (“group letter”), supported the Board’s proposal on ECIs. The Reserve Bank commenter noted that it is aware that some advocates support allowing ECIs to be handled in the same manner as checks and has worked with these advocates to explore the possibility of making legal and operational changes to support ECIs. However, the Reserve Bank commenter stated that there is currently no consensus among industry participants to change laws or adopt standards necessary to support ECIs. In the absence of such laws and standards supporting ECIs, the Reserve Bank commenter believes that ECIs represent an unacceptable level of risk to financial institutions. Similarly, the group letter stated that ECIs lack legal status under existing laws and expose financial institutions to risks that cannot be effectively mitigated. The group letter stated that due to ECIs uncertain legal status, it is important to protect financial institutions that receive ECIs during the check collection process from damage or loss arising from the fact that ECIs are not derived from paper checks. Therefore, the group supported the Board’s proposal to allow Reserve Banks to require senders to provide warranties and indemnities with respect to ECIs and did not support additional rulemaking to allow the handling of ECIs by the Reserve Banks.

Fourteen commenters, including a joint commenter letter submitted by businesses, financial institutions, and industry associations (“joint letter”), generally did not support the Board’s proposed amendments on ECIs. The joint letter stated that the Board’s proposal

concerning ECIs is not in line with the Board's recent payment system improvement efforts.⁶ Another commenter stated that the Board's proposal limited consumer choice because ECIs may be initiated by consumers that do not have access to a debit or credit card. Commenters stated that the Board's proposal discouraged the evolution of the check system to an all-electronic payment system that would result in lower barriers to entry, lower cost, increased speed, and increased parity among financial institutions. Two commenters requested the Board to conduct further studies on ECIs. One commenter expressed concern that institutions would be unable to identify ECIs and requested that the Board provide guidance on how banks can recognize ECIs. Another commenter requested that the Board expressly set out rules for alternative methods of direct exchange of ECIs in its final rule and guidance.

The Board has considered the comments received and has adopted the amendments concerning ECIs as proposed in its final rule. The Board notes that numerous comments erroneously viewed the Board's proposed amendments as substantive modifications that created a new prohibition on ECIs. However, as discussed above, ECIs are not "items" under the Board's current Regulation J and therefore cannot be handled by the Reserve Banks. This exclusion of ECIs under current Regulation J is already reflected in current OC 3, which requires that an "electronic item" contain an image and data captured from a paper check. The Board's amendments to the definition of "item" are intended only to provide additional clarity regarding these existing exclusions and do not create any new prohibitions. The Board believes this existing exclusion shifts liability to parties better positioned to know whether a

⁶ The joint letter specifically cited the Federal Reserve's 2013 consultation paper. The Federal Reserve Banks, Payment System Improvement – Public Consultation Paper (2013).

purported item is electronically created and that can either prevent the ECI from entering the check-collection system or assume the risk of sending it forward. Moreover, the Board's amendments would not prevent entities that desire to exchange ECIs from doing so by agreement using direct exchange relationships or other methods not involving the Reserve Banks.

The Board appreciates comments regarding the Federal Reserve's payment system improvement efforts and continues to support technological innovation in the payments system. However, as set forth in the Federal Reserve's *Strategies for Improving the U.S. Payment System* paper,⁷ the Federal Reserve is committed to improving the speed and efficiency of the U.S. payment system from end-to-end while maintaining a high level of safety and accessibility. As explained in that paper, "credit-push payments," which allow the paying bank to authenticate the customer and confirm "good funds" are available to support the transaction, have become the expectation when making electronic person-to-person, business-to-business and certain bill payments. Unlike "credit-push payments," "debit-pull payments" such as ECIs have a higher risk profile because they generally do not have the same authentication processes and may allow unauthorized parties who have access to a payer's account information to fraudulently pull funds out of the payer's account. To date, there has not been the industry support or necessary investment to address the heightened risk profiles created by processing electronically-created debit instruments through the check collection system. Moreover, there is legal uncertainty as to the status of ECIs that are

⁷ Federal Reserve System, *Strategies for Improving the U.S. Payment System* (2016).

processed as if they were checks under the U.C.C. and the Electronic Funds Transfer Act. The Board believes that the heightened risk profile and legal uncertainty surrounding ECIs currently outweigh the potential benefits of ECIs mentioned by the commenters and, accordingly, will not conduct further studies on ECIs at this time.

The Board does not believe it is appropriate to adopt guidance to clarify how banks can distinguish ECIs from electronic checks. As it stated in its proposal, the Board recognizes that a bank receiving an electronic image generally cannot distinguish an image that is derived from a paper check from an ECI. This inability to distinguish ECIs from electronic images of paper checks is the reason the Board adopted indemnities with respect to ECIs in Regulation CC. The parties in the best position to know whether a purported item is electronically created are also in the best position to assess and take on any associated risks that may arise from ECIs entering the check collection system and can also address such risk in agreements with their customers that deposit ECIs.

C. Settlement and Payment

Regulation J currently provides that settlement with a Reserve Bank for cash items “shall be made by debit to an account on the Reserve Bank’s books, cash, or other form of settlement” to which the Reserve Bank has agreed.⁸ With respect to noncash items, Regulation J provides that a Reserve Bank may require settlement by cash, by a debit to an account on a Reserve Bank’s books or “by any of the following that is in a form acceptable to the collecting Reserve Bank: bank draft, transfer of funds or bank credit, or any other form of

⁸ 12 CFR 210.9(b)(5).

payment authorized by State law.”⁹ Regulation J also currently provides that a Reserve Bank may require a nonbank payor to settle for items by cash, or by “any of the following that is in a form acceptable to the Reserve Bank: cashier’s check, certified check, or other bank draft or obligation.”¹⁰ In order to facilitate the efficient collection of items, the Reserve Banks’ current practice is generally to settle for items by debit to an account on the Reserve Bank’s books. The use of cash is rare, typically only done in emergency situations, and could be covered by a provision allowing “other form of settlement to which the Reserve Bank agrees.”

The Board proposed to revise certain settlement provisions of Regulation J to remove references to cash and other specified forms of settlement (e.g., cashier’s checks or certified checks) and instead state that the Reserve Banks may settle by a debit to an account on the Reserve Bank’s books, or another form of settlement acceptable to the Reserve Banks. The Board requested comment on possible implications that the proposed changes may have on financial institutions with which the Reserve Banks settle for the presentment of items.

The Board received one comment supporting the proposal and no opposing comments. The Board has adopted these amendments as proposed in the final rule.

D. Legal status of terms used in financial messaging standards

Financial messaging standards provide a common format that allows different financial institutions to communicate. The Board has separately requested comment on the Federal Reserve Banks’ plan to migrate to the ISO 20022 financial messaging standard for the

⁹ 12 CFR 210.9(c).

¹⁰ 12 CFR 210.9(d).

Fedwire Funds Service.¹¹ ISO 20022 is an international standard that employs terminology that differs in key respects from that used in U.S. funds-transfer law, including Regulation J. The Board proposed an amendment to subpart B of Regulation J that would clarify that terms used in financial messaging standards, such as ISO 20022, do not confer or connote legal status or responsibilities.

The Board received four comments supporting these proposed changes and no opposing comments. The Board has adopted these amendments as proposed.

III. Section-by-Section Analysis

Subpart A – Collection of Checks and Other Items by Federal Reserve Banks

Section 210.2 Definitions

1. Section 210.2(h) – Check

Regulation J defines the term “check” as a draft as defined in the U.C.C. drawn on a bank and payable on demand. The Board proposed to revise the definition of “check” to mean a “check” and an “electronic check” as those terms are defined in Regulation CC. This amendment aligns the terminology in the two regulations.

Regulation J also includes the term “check as defined in 12 CFR 229.2(k)” (the Regulation CC definition of “check”). This term is used in Regulation J in those provisions that require specific references to the Regulation CC definition of “check.” (See §§ 210.2(m), 210.7(b)(2), and 210.12(a)(2).) The Board proposed to delete the definition of “check as defined in 12 CFR 229.2(k)” because it was no longer needed in light of the

¹¹ 83 FR 31391 (July 5, 2018).

proposed revision of the Regulation J definition of “check” to cross-reference the Regulation CC definition. The Board also proposed to revise the three provisions where it is used by deleting the reference to “check as defined in 12 CFR 229.2(k).”

Six commenters, including the group letter, were generally supportive of the Board’s proposed changes to align Regulation J with Regulation CC. The Board did not receive specific comments on proposed § 210.2(h) or any opposing comments. The Board has adopted these changes as proposed.

2. Section 210.2(i) – Item

Regulation J uses the term “item” to refer to the instruments and electronic images that the Reserve Banks handle. Regulation J uses the term “electronic item” to refer to an electronic image of an item, and information describing that item, that a Reserve Bank agrees to handle as an item pursuant to an operating circular. To align the terminology of Regulation J with Regulation CC, the Board proposed to delete the definition of “electronic item” and revise the definition of “item” in § 210.2(i) to include a check, which, under the proposed amendment discussed above would include both a check and an electronic check as defined in Regulation CC. The Board also proposed to add a clarifying statement that the term “item” does not include an ECI as defined in § 229.2 of Regulation CC.

Six commenters, including the group letter, were generally supportive of alignment between Regulation J and Regulation CC. With respect to ECIs in particular, three commenters supported the Board’s proposed amendments, while fourteen commenters generally opposed amendments that restricted the Reserve Banks’ handling of ECIs. For reasons described in the overview section, the Board has adopted § 210.2(i) as proposed.

3. Section 210.2(m) – Returned Check

Current § 210.2(m) defines a “returned check” as “a cash item or a check as defined in 12 CFR 229.2(k) returned by a paying bank.” To align the definition of “returned check” with “check,” the Board proposed to delete the reference to “check as defined in 12 CFR 229.2(k)” and instead refer to the definition of “electronic returned check” in Regulation CC. The Board did not receive any comments on proposed § 210.2(m). The Board has adopted these changes as proposed.

4. Section 210.2(n) – Sender

A “sender” under § 210.2(n) is any of several listed entities that sends an item to a Reserve Bank for forward collection. The Board proposed to add “member bank, as defined in section 1 of the Federal Reserve Act” in § 210.2(n)(2) to include a bank or trust company that is a member of one of the Federal Reserve Banks to ensure inclusion of any member bank that does not fall under the existing definition. The Board proposed to redesignate current § 210.2(n)(2)-(6) to § 210.2(n)(3)-(7) to accommodate the insertion.

One commenter requested that the Board clarify whether its proposed changes to § 210.2(n) would expand the types of institutions that may directly participate as a sender in the Fedwire services subject to subpart B of Regulation J, such as nondepository trust companies. The commenter noted that revising the definition of sender to capture member nondepository trust companies would prompt concerns regarding payment system risk with respect to access to Federal Reserve financial services. The Board’s proposed changes to the definition of “sender” does not affect the rights of any particular type of entity to obtain access to Federal Reserve services. (In any case, the definition of “sender” in § 210.2(n) applies only to the collection of checks and other items by the Reserve Banks and not to the Fedwire Funds Service.) As stated in the Board’s proposal, proposed § 210.2(n) is intended to ensure

inclusion of any member bank that does not fall under the existing list of entities that send items to a Reserve Bank for forward collection. Whether any particular member bank, including a nondepository trust company, obtains an account and access to Reserve Bank check services continues to be governed by existing laws, rules, and policies, including the Federal Reserve Act, the Board's Policy on Payment System Risk and the Reserve Banks' internal risk analysis. The Board intends no expansion of rights by this technical change. The Board has adopted the amendments as proposed.

5. Section 210.2(q) – Fedwire

Current § 210.2(q) defines “Fedwire” as having the same meaning set forth in § 210.26(e). The Board proposed to amend this definition to refer to both “Fedwire Funds Service and Fedwire” to conform to the proposed amendment to § 210.26(e). The Board did not receive any comments on proposed § 210.2(q) and has adopted the revisions as proposed.

Section 210.3 General Provisions

Section 210.3(a) provides general provisions concerning the obligations of Reserve Banks and the role of operating circulars. As discussed in the overview section on ECIs, the Board proposed to add a sentence to § 210.3(a) to permit Reserve Banks to require a sender to provide warranties and indemnities that only items and any noncash items the Reserve Banks have agreed to handle will be sent to the Reserve Banks. Additionally, in order to allow the Reserve Banks to pass any such warranties and indemnities forward, the Board proposed to authorize the Reserve Banks to provide to a subsequent collecting bank and to the paying bank any warranties and indemnities provided by the sender pursuant to this paragraph.

The Board received one comment, the group letter, supporting the proposal. The Board did not receive any comments opposing these particular amendments, although as

discussed in the overview section, fourteen commenters generally opposed amendments that restricted the Reserve Banks' handling of ECIs. For the reasons described in the overview section, the Board has adopted these revisions as proposed.

Section 210.4 Sending items to Reserve Banks

Section 210.4(a) sets forth the rule for determining the Reserve Bank to which an item should be sent. The Board proposed to clarify this paragraph to provide that a sender's Administrative Reserve Bank may direct a sender (other than a Reserve Bank) to send any item to a specified Reserve Bank, whether or not the item is payable in the Reserve Bank's district. This amendment reflects current practice in the Reserve Banks' check service and is not expected or intended to have a substantive effect. The Board also proposed to capitalize the term "Administrative Reserve Bank" wherever it appears to conform to the defined term in § 210.2(c).

The Board did not receive any comments on proposed § 210.4 and has adopted the revisions as proposed.

Section 210.5 Sender's agreement; recovery by Reserve Bank

1. Section 210.5(a) – Sender's agreement

Current § 210.5(a) lists the warranties, authorizations, and agreements made by a sender. The first two paragraphs (current § 210.5(a)(1) and (2)) apply to all items and require the sender to authorize the Reserve Banks to handle the item sent and warrant that the sender is entitled to enforce the item, that the item has not been altered, and that the item bears the indorsements applied by all prior parties. The Board did not propose to revise these paragraphs. Current § 210.5(a)(3) and (4) set out warranties for electronic items and electronic items that are not representations of substitute checks, respectively. These

warranties are now specified in Regulation CC, and the Board proposed to revise Regulation J accordingly. Specifically, the Board proposed to amend § 210.5(a)(3) to require the sender to make all applicable warranties and indemnities set forth in Regulation CC and the U.C.C. The proposal retained the existing requirement that the sender make all warranties set forth in and subject to the terms of U.C.C. 4-207 for an electronic check as if it were an item subject to the U.C.C. The proposed changes were intended to streamline Regulation J, align § 210.5(a) with the Regulation CC provisions that set out warranties and indemnities for electronic checks, and ensure a seamless chain of warranties for the items handled by the Reserve Banks.

The Board also proposed to require a sender to make any warranties or indemnities regarding the sending of items that the Reserve Banks include in an operating circular issued in accordance with § 210.3(a) to ensure that only items and any noncash items the Reserve Banks have agreed to handle will be sent to the Reserve Banks (proposed § 210.5(a)(4)). Finally, the Board proposed to add a reference to “indemnities” to the introductory text of § 210.5(a) to reflect the coverage of sender indemnities in proposed § 210.5(a)(3) and (4).

One commenter, the group letter, requested that the Board add commentary concerning the cross referencing of Regulation CC’s image quality warranty. Under Regulation CC, each bank that transfers an electronic check warrants that “the electronic image accurately represents all of the information on the front and back of the original check as of the time the original check was truncated and the electronic information includes an accurate record of all MICR line information required for a substitute check under § 229.2(aa)

and the amount of the check.”¹² The group letter requests that the Board add commentary in Regulation J to clarify that the warranty does not require that the electronic check capture those characteristics of the paper check, such as watermarks, microprinting, or other physical security features, that cannot survive the imaging process.

The Board acknowledges that the warranty in § 229.34(a)(1)(i) does not require that the electronic check capture those characteristics of the paper check that cannot survive the imaging process. The commentary to § 229.34(a)(1)(i) states that the electronic check warranties correspond to the warranties made by a bank that transfers, presents, or returns a substitute check.¹³ The commentary to the corresponding substitute check warranty states “a substitute check need not capture other characteristics of the check, such as watermarks, microprinting, or other physical security features that cannot survive the imaging process or decorative images, in order to meet the accuracy requirement.”¹⁴ The Board’s amendments to Regulation J requiring the sender to make all applicable warranties and indemnities set forth in Regulation CC also cross reference the relevant commentary in Regulation CC. Accordingly, the Board does not believe it is necessary to add additional commentary in Regulation J and adopts the revisions as proposed.

¹² 12 CFR 229.34(a)(1)(i).

¹³ See Regulation CC, Official Staff Commentary Section 229.34(a)-2.

¹⁴ See Regulation CC, Official Staff Commentary Section 229.51(a)-3; *see also First Am. Bank v. Fed. Reserve Bank of Atlanta*, 842 F.3d 487 (7th Cir. 2016).

2. Section 210.5(a)(5) – Sender’s liability to Reserve Bank

Current § 210.5(a)(5) sets out the sender’s liability to Reserve Banks. The Board proposed to amend this paragraph to align this paragraph to changes elsewhere in the proposed rule.

Current § 210.5(a)(5)(i)(C) states that the sender agrees to indemnify the Reserve Bank for any loss or expense resulting from “[a]ny warranty or indemnity made by the Reserve Bank under § 210.6(b), part 229 of this chapter, or the U.C.C.” The Board proposed to amend this provision to provide that the sender will also indemnify a Reserve Bank for any loss or expense sustained resulting from any warranties and indemnities regarding the sending of “items” required by the Reserve Bank in an operating circular issued pursuant to proposed § 210.3(a).

Current § 210.5(a)(5)(ii) specifies conditions and limitations to a sender’s liability for warranties and indemnities that a Reserve Bank makes for a substitute check, a paper or electronic representation thereof, or any other electronic item. The Board proposed to delete the term “electronic item” in current § 210.5(a)(5)(ii) and replace it with “electronic check.”

Current § 210.5(a)(5)(ii)(A) provides that a sender of an original check is not liable for any amount that the Reserve Bank pays under subpart D of Regulation CC for a subsequently created substitute check or under § 210.6(b)(3) for an electronic item, absent the sender’s agreement to the contrary. The Board proposed to delete the reference to current § 210.6(b)(3), which lists warranties and an indemnity for an electronic item that is not a representation of a substitute check, and replace it with a reference to § 229.34 of Regulation CC with respect to an electronic check, consistent with other proposed amendments to § 210.6(b) described below.

Current § 210.5(a)(5)(ii)(B) provides that nothing in Regulation J alters the liability structure that applies to substitute checks and paper or electronic representations of substitute checks under subpart D of Regulation CC. The Board proposed to add that this subpart also does not alter the liability of a sender of an electronic check under § 229.34 of Regulation CC, consistent with the other proposed revisions to Regulation J.

Current § 210.5(a)(5)(ii)(C) provides that a sender of an electronic item that is not a representation of a substitute check is not liable for any related warranties or indemnities that a Reserve Bank pays that are attributable to the Reserve Bank's own lack of good faith or failure to exercise ordinary care. The Board proposed to broaden this provision by applying the limitation on liability to all senders for any amount that the Reserve Bank pays that is attributable to the Reserve Bank's own lack of good faith or failure to exercise ordinary care under Regulation J or Regulation CC. The Board proposed to redesignate this paragraph as § 210.5(a)(5)(iii) and make conforming changes to cross-references.

The Board did not receive any comments on proposed § 210.5(a). As discussed in the overview section, the Board received numerous comments generally supporting aligning Regulation J with Regulation CC. The Board has adopted these revisions as proposed.

3. Section 210.5(c) & (d) – Recovery by Reserve Bank and Methods of recovery

Section 210.5(c) sets out the procedures by which a Reserve Bank may recover against a sender if certain actions or proceedings related to the sender's actions are brought against (or defense is tendered to) a Reserve Bank. A portion of this paragraph was inadvertently dropped from the Code of Federal Regulations. The Board proposed to reinstate the dropped language, which provides that, upon entry of a final judgment or decree, a Reserve Bank may recover from the sender the amount of attorneys' fees and other expenses of litigation

incurred, as well as any amount the Reserve Bank is required to pay because of the judgment or decree or the tender of defense, with interest. In addition, the Board proposed to correct cross-references to this provision in § 210.5(d).

The Board did not receive any comments on proposed § 210.5(c) & (d). The Board has adopted these revisions as proposed.

4. Section 210.5(e) – Security interest

Current § 210.5(e) provides that when a sender sends an item to a Reserve Bank, the sender and any prior collecting bank grant to the sender's Administrative Reserve Bank a security interest in all of their respective assets in the possession of, or held for the account of, any Reserve Bank to secure their respective obligations due or to become due to the Administrative Reserve Bank under this subpart or subpart C of part 229 (Regulation CC). The Board proposed to amend this paragraph to refer to subpart D of Regulation CC in addition to subpart C, as senders may have obligations to Reserve Banks under that subpart as well.

The Board did not receive any comments on proposed § 210.5(e). The Board has adopted these revisions as proposed.

Section 210.6 Status, warranties, and liability of Reserve Bank

1. Section 210.6(a)(2) – Limitations on Reserve Bank liability

Section 210.6(a)(2) limits a Reserve Bank's liability with respect to an item to three instances: (1) the Reserve Bank's own lack of good faith or failure to exercise ordinary care, (2) as provided in this section of Regulation J, and (3) as provided in subparts C and D of Regulation CC. The Board proposed to expand this list to provide that a Reserve Bank may

be liable under any warranties and indemnities provided in an operating circular issued in accordance with § 210.3(a) regarding the sending of items.

The Board received one comment, the group letter, supporting its proposal to allow the Reserve Banks to address warranties and indemnities for eligible items and non-cash items in the operating circular. The Board did not receive any opposing comments. The Board has adopted these revisions as proposed.

2. Section 210.6(b) – Warranties and liability

Section 210.6(b) sets forth the warranties and indemnities made by a Reserve Bank when it presents or sends an item. In alignment with the Board's proposed amendments to the sender's warranties in § 210.5(a), the Board proposed to replace current § 210.6(b)(2) and (3), which provide warranties and indemnities for electronic items and electronic items that are not representations of substitute checks, respectively. Those warranties are now covered by Regulation CC. The Board also proposed to make a conforming amendment to § 210.6(b)(1)(iii) to eliminate the unnecessary reference to "paper or electronic form."

The Board proposed a new § 210.6(b)(2) to provide that a Reserve Bank would make any warranties or indemnities regarding the sending of items as set forth in an operating circular issued pursuant to proposed § 210.3(a). This language corresponds to the similar proposed provision for sender liability in § 210.5(a)(4).

The Board proposed a new § 210.6(b)(3) to provide that the Reserve Bank makes to a subsequent collecting bank and to the paying bank all the warranties and indemnities set forth in subparts C and D for Regulation CC. Proposed § 210.6(b)(3) would retain the existing application of U.C.C. 4-207 warranties to electronic items (now called electronic checks).

In § 210.6(b)(4), the Board proposed to retain the existing Reserve Bank indemnity for substitute checks created from electronic checks, which is in current § 210.6(b)(3)(ii). This provision provides an indemnity chain for substitute check indemnity claims under Regulation CC, enabling receiving banks (and, in turn, Reserve Banks) to pass the loss on such claims to the bank whose choice to handle an item electronically necessitated the later creation of a substitute check.

The Board received one comment, the group letter, on proposed § 210.6(b)(3). The group letter noted that the persons that receive the electronic check warranties from the Reserve Banks appeared to be more limited than the persons that receive the electronic check warranties under Regulation CC. Specifically, proposed § 210.6(b)(3) does not extend the electronic check warranties to the drawer of the check on the forward side, unlike the warranties in Regulation CC. The group letter noted, however, that proposed § 210.6(a)(2)(iv) provides that a Reserve Bank does not assume any liability with respect to an item or its proceeds “except as provided under subparts C and D of Regulation CC.” The group letter requested that the Board clearly require that the Reserve Banks provide the same scope and recipients of the new electronic check warranties in Regulation J as provided under Regulation CC.

The Board agrees with the group letter that Reserve Banks should provide the electronic check and electronic returned check warranties to the same scope of recipients in Regulation J as in Regulation CC, including to drawers and owners of checks. The Board believes that extending the warranties to the drawers and owners is consistent with the warranty flow set forth in section 5 of the Check 21 Act for substitute checks and will protect parties outside the banking system from any undesirable consequences resulting from check

truncation. The Board has revised proposed § 210.6(b)(3) accordingly in the final rule. Otherwise, the Board has adopted § 210.6(b) as proposed, with minor revisions to correct typographical errors in § 210.6(b)(2) & (3).

3. Section 210.6(c) – Limitation on liability

The limitations on Reserve Bank liability are set forth in proposed (and current) § 210.6(a)(2). The Board proposed to delete paragraph (c) as it is redundant and to redesignate current paragraph (d) as paragraph (c). The Board did not receive any comments on proposed § 210.6(c). The Board has adopted these revisions as proposed.

Section 210.7 Presenting items for payment

Section 210.7(b) provides the places of presentment for a Reserve Bank or subsequent collecting bank. Current § 210.7(b)(2) states “In the case of a check as defined in 12 CFR 229.2(k), in accordance with 12 CFR 229.36.” In alignment with the Board’s proposed deletion of the defined term “check as defined in 12 CFR 229.2(k),” the Board proposed to delete the use of that term in § 210.7(b)(2), as it is no longer needed, and make other minor edits.

The Board did not receive any comments on proposed § 210.7. The Board has adopted these revisions as proposed.

Section 210.9 Settlement and payment

1. Section 210.9(b)(5), (c), and (d) – Manner of settlement, Noncash items, and Nonbank payor

Current § 210.9(b)(5) requires that settlement for cash items with a Reserve Bank be made by debit to an account on the Reserve Bank’s books, cash, or other form of settlement to which the Reserve Bank agrees. The Board proposed to amend this provision by removing the reference to cash as a means of settlement. The Board also proposed to make conforming

amendments to § 210.9(c) and (d), as well as to remove the references to other rarely-used forms of settlement (cashier's checks, certified checks, or other bank drafts or obligations). The Board proposed to correct cross-references and to capitalize the term "Administrative Reserve Bank" wherever it appears to conform to the defined term in § 210.2(c).

As discussed in the overview section, the Board received one comment, the group letter, supporting the proposal. The Board did not receive any opposing comments. The Board has adopted the revisions as proposed.

2. Section 210.9(e) – Handling of payment

Current § 210.9(e) states that a Reserve Bank may handle a bank draft or other form of payment it receives in payment of a cash item as a cash item and that a Reserve Bank may handle a bank draft or other form of payment it receives in payment of a noncash item as either a cash item or a noncash item. The Board proposed to delete this paragraph as it is now obsolete.

The Board did not receive any comments on proposed § 210.9(e) and has deleted this paragraph as proposed.

3. Section 210.9(f) – Liability of Reserve Bank

Current § 210.9(f) states that a Reserve Bank that acts in good faith and exercises ordinary care shall not be liable for the nonpayment of, or failure to realize upon, any bank draft or other form of payment that it accepts pursuant to § 210.9(b)-(d). The Board proposed to renumber this paragraph as § 210.9(e) and to replace the reference to "bank draft or other form of payment" with "any non-cash form of payment" to conform to the proposed changes to the other provisions of this section.

The Board did not receive any comments on proposed § 210.9(f). The Board has adopted these revisions as proposed.

Section 210.10 Time schedule and availability of credits for cash items and returned checks

Section 210.10(a) states that each Reserve Bank shall “include in its operating circulars” its time schedules for availability of cash items and returned checks and, correspondingly, when credits can be counted toward reserve balance requirements for purposes of Regulation D (12 CFR part 204). The Reserve Banks’ practice is to publish the time schedules on the Federal Reserve website for financial services. Accordingly, the Board proposed to amend this paragraph to delete the requirement that time schedules be included in the operating circulars and, instead, require only that the time schedules be published.

The Board did not receive any comments on proposed § 210.10. The Board has adopted these revisions as proposed.

Section 210.11 Availability of proceeds of noncash items; time schedule

1. Section 210.11(b) – Time Schedule

Section 210.11(b) states that a Reserve Bank may give credit for the proceeds of a noncash item subject to payment in actually and finally collected funds in accordance with a time schedule included in its operating circulars. To conform to amendments made in proposed § 210.10, the Board proposed to delete the reference to operating circulars and require only that the time schedule be published.

The Board did not receive any comments on proposed § 210.11(b). The Board has adopted these revisions as proposed.

2. Section 210.11(c) – Handling of payment

Current § 210.11(c) prohibits a Reserve Bank from providing credit for a bank draft or other form of payment for a noncash item until it receives payment in actually and finally collected funds. The Board proposed to delete this paragraph, as actually and finally collected funds are already required by § 210.11(a).

The Board did not receive any comments on proposed § 210.11(c) and has adopted these revisions as proposed.

Section 210.12 Return of cash items and handling of returned checks

Section 210.12 sets out provisions governing the handling of returned checks. It is the counterpart to §§ 210.5 and 210.6, which govern the handling of items for forward collection.

1. Section 210.12(a) – Return of items

Current § 210.12(a)(2) sets out the procedures by which a paying bank may return checks not handled by Reserve Banks and refers to “check as defined in § 229.2(k) of this chapter (Regulation CC).” In alignment with the Board’s proposal to delete the defined term “check as defined in § 229.2(k)” in § 210.2(h), the Board proposed to delete the use of this term in this paragraph, as it is no longer needed, and to use the term “check” instead.

The Board did not receive any comments on proposed § 210.12(a) and has adopted these revisions as proposed.

2. Section 210.12(c) – Paying bank’s and returning bank’s agreement

Current § 210.12(c) provides the warranties, authorizations, and agreements related to returned checks made by paying banks and returning banks. The Board proposed amendments to this paragraph that are parallel to the proposed amendments for forward-collection items with respect to the liability of the sender (§ 210.5(a)(3)) and the Reserve Banks (§210.6(b)(2)). Specifically, the Board proposed to replace current § 210.12(c)(3) and

(4), which provide warranties for all returned checks that are electronic items and warranties for returned checks that are electronic items that are not representations of substitute checks, respectively, with a provision that requires the paying bank or returning bank to make all the warranties and indemnities as set forth in Regulation CC, as applicable (proposed § 210.12(c)(3)).

Current § 210.12(c)(5) sets out the conditions under which a paying bank or returning bank is liable to a Reserve Bank. The Board proposed to redesignate this paragraph as § 210.12(c)(4) and amend the paragraph to correspond with the proposed amendments to the section on sender's liability to a Reserve Bank (§ 210.5(a)(4)). The proposed amendments were intended to create consistent liability provisions for senders, paying banks, and returning banks.

The Board did not receive any comments on proposed § 210.12(c) and has adopted these revisions as proposed, with a minor revision to correct a typographical error in § 210.12(c)(1).

3. Section 210.12(d) – Liability under other law

Current § 210.12(d) is titled “Preservation of other warranties and indemnities.” The Board proposed to change the title of this paragraph to “Returning bank's or paying bank's liability under other law” to mirror the heading for the corresponding paragraph for senders (§ 210.5(b)).

The Board did not receive any comments on proposed § 210.12(d). The Board has adopted these revisions as proposed.

4. Section 210.12(e) – Warranties by and liability of Reserve Bank

Current § 210.12(e) sets forth a Reserve Bank's liability when it handles a returned check, including warranties and liabilities. The Board proposed to amend this paragraph to correspond to the amendments proposed in § 210.6(b) related to the warranties and liabilities that are made by Reserve Banks when presenting or sending an item.

The Board received one comment, the group letter, on proposed § 210.12(e). Corresponding to the comment discussed in the section-by-section analysis for § 210.6(b)(3), the group letter stated that the proposed Regulation J does not extend the electronic check warranties for returns to the owner of the check, unlike the warranties in Regulation CC. The group letter requested that the Board require the Reserve Banks provide in Regulation J the same scope and recipients of the new electronic check warranties as provided under Regulation CC.

For the reasons described in the section-by-section analysis for § 210.6(b), the Board has revised proposed § 210.12(e)(ii) to extend the warranties for electronic returned checks provided by Reserve Banks to the same scope of recipients as provided in Regulation CC. The Board has also revised proposed § 210.12(e)(2)(i) to correct a typographical error.

5. Section 210.12(f) & (g) – Recovery by Reserve Bank & Methods of recovery

Section 210.12(f) parallels § 210.5(c) and sets out the procedures by which a Reserve Bank may recover against a paying bank or returning bank if certain actions or proceedings related to the paying bank's or returning bank's actions are brought against (or defense is tendered to) a Reserve Bank. A portion of this paragraph was inadvertently dropped from the Code of Federal Regulations. The Board proposed to reinstate the dropped language, which provides that, upon entry of a final judgment or decree, a Reserve Bank may recover from the paying bank or returning bank the amount of attorneys' fees and other expenses of litigation

incurred, as well as any amount the Reserve Bank is required to pay because of the judgment or decree or the tender of defense, with interest. In addition, the Board proposed to correct cross-references and make organizational changes in § 210.12(g).

The Board did not receive any comments on proposed § 210.12(f) & (g) and has adopted these revisions as proposed.

Subpart B – Funds Transfers Through Fedwire

Section 210.25 Authority, Purpose, and Scope

Section 210.25 sets out the authority, purpose, and scope for subpart B of Regulation J, which governs Fedwire funds transfers. The Board proposed to add a new § 210.25(e) to clarify that financial messaging standards (e.g., ISO 20022), including the financial messaging components, elements, technical documentation, tags, and terminology used to implement those standards, do not confer or connote legal status or responsibilities. The proposed amendment would specify that Regulation J, Article 4A of the U.C.C., and the operating circulars of the Reserve Banks govern the rights and obligations of parties to the Fedwire Funds Service and supersede any inconsistency between a financial messaging standard adopted by the Fedwire Funds Service. The proposal would also make a conforming change to § 210.25(b)(2). Additionally, the Board proposed to add in the commentary examples of inconsistent terminology between the ISO 20022 financial messaging standard and U.S. funds transfer law.

The Board received four comments supporting these proposed changes and no opposing comments. The Board has adopted these amendments as proposed.

Section 210.26 Definitions

Section 210.2(e) defines the term “Fedwire” to mean the funds-transfer system owned and operated by the Federal Reserve Banks that is used primarily for the transmission and settlement of payment orders governed by subpart B. The Board proposed to amend this definition so that it applies to the official title of the service, “Fedwire Funds Service,” as well as the shorthand term “Fedwire.” The Board also proposed to change references to “Fedwire” to “Fedwire Funds Service” in §§ 210.9(b)(4)(i), 210.25(a) and (b)(3), and 210.29(b).

The Board did not receive any comments on proposed § 210.26 and has adopted these revisions as proposed.

Section 210.32 Federal Reserve Bank Liability; Payment of Interest

Current § 210.32 sets out provisions that govern Federal Reserve Bank liability and payment of interest. Section 210.32(b) provides that compensation that is paid by Federal Reserve Banks in the form of interest shall be calculated in accordance with section 4A-506 of Article 4A. Under section 4A-506(a), the amount of interest may be determined by agreement between the sender and receiving bank or by funds-transfer system rule. If there is no such agreement, under section 4A-506(b), the amount of interest is based on the federal funds rate. The current commentary to § 210.32(b) states that “Interest would be calculated in accordance with the procedures specified in section 4A-506(b).” The Board proposed to delete this statement and rearrange the commentary to clarify that interest can be calculated in accordance with both section 4A-506(a) and (b).

The Board did not receive any comments on the proposed commentary to § 210.32. The Board has adopted these revisions as proposed.

IV. Competitive Impact Analysis

The Board conducts a competitive impact analysis when it considers an operational or legal change, if that change would have a direct and material adverse effect on the ability of other service providers to compete with the Federal Reserve in providing similar services due to legal differences or due to the Federal Reserve's dominant market position deriving from such legal differences. All operational or legal changes having a substantial effect on payments-system participants will be subject to a competitive-impact analysis, even if competitive effects are not apparent on the face of the proposal. If such legal differences exist, the Board will assess whether the same objectives could be achieved by a modified proposal with lesser competitive impact or, if not, whether the benefits of the proposal (such as contributing to payments-system efficiency or integrity or other Board objectives) outweigh the materially adverse effect on competition.¹⁵

The Board does not believe that the amendments to Regulation J will have a direct and material adverse effect on the ability of other service providers to compete effectively with the Reserve Banks in providing similar services due to legal differences. The final rule would align the provisions in Regulation J governing Reserve Bank services to the generally applicable provisions in Regulation CC. The final rule would not affect the competitive position of private-sector presenting banks vis-à-vis the Reserve Banks.

V. The Riegle Community Development and Regulatory Improvement Act of 1994

The Riegle Community Development Regulatory Improvement Act of 1994 requires that agency regulations that impose additional reporting, disclosure, and other requirements

¹⁵ Federal Reserve Regulatory Service, 7-145.2.

on insured depository institutions take effect on the first calendar quarter following publication in final form, unless the agency determines for good cause that the regulation should become effective before such time. 12 U.S.C. 4802(b). Consistent with the Riegle Community Development Act, this final rule is effective on January 1, 2019.

VI. Paperwork Reduction Act

In accordance with the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. 3506; 5 CFR part 1320, appendix A.1), the Board may not conduct or sponsor, and a respondent is not required to respond to, an information collection unless it displays a valid Office of Management and Budget (OMB) control number. The Board reviewed the final rule under the authority delegated to the Board by the OMB and determined that it contains no collections of information under the PRA.¹⁶ Accordingly, there is no paperwork burden associated with the rule.

VII. Regulatory Flexibility Act

An initial regulatory flexibility analysis (IRFA) was included in the proposal in accordance with section 3(a) of the Regulatory Flexibility Act (RFA), 5 U.S.C. 601 et seq. (RFA). In the IRFA, the Board requested comment on the effect of the proposed rule on small entities and on any significant alternatives that would reduce the regulatory burden on small entities. The Board did not receive any comments. The RFA requires an agency to prepare a final regulatory flexibility analysis (FRFA) unless the agency certifies that the rule will not, if promulgated, have a significant economic impact on a substantial number of small

¹⁶ See 44 U.S.C. 3502(3).

entities. In accordance with section 3(a) of the RFA, the Board has reviewed the final regulation. Based on its analysis, and for the reasons stated below, the Board certifies that the rule will not have a significant economic impact on a substantial number of small entities.

The final rule will apply to all depository institutions regardless of their size.¹⁷ Pursuant to regulations issued by the Small Business Administration (13 CFR 121.201), a “small banking organization” includes a depository institution with \$550 million or less in total assets. Based on call report data, there are approximately 9,631 depository institutions that have total domestic assets of \$550 million or less and thus are considered small entities for purposes of the RFA. The Board’s final rule generally does not have any projected reporting, recordkeeping or other compliance requirements, as the revisions to Regulation J align the rights and obligations of sending banks, paying banks, and Federal Reserve Banks (Reserve Banks) with the Board’s recent amendments to Regulation CC. The final rule’s warranties and indemnities are similar to the warranties and indemnities that apply to paper and electronic checks under existing Regulation J and other law. The final rule does not require any bank to change the form in which it submits checks, nor do they require any bank to submit reports, maintain records, or provide notices or disclosures.

With respect to ECIs, provisions in the final rule would allow the Reserve Banks to require that senders provide certain warranties and indemnities. The Board recognizes these provisions may affect the creation and acceptance of ECIs by small entities. Neither Regulation J nor Regulation CC would prevent private-sector collecting banks from doing the

¹⁷ The final rule would not impose costs on any small entities other than depository institutions.

same. In addition, the Board's final rule would not prevent small entities that desire to exchange ECIs from doing so by agreement using direct exchange relationships or other methods not involving the Reserve Banks. The Board believes the final rule will help to shift liability to parties better positioned to know whether an item is electronically created and that can either prevent the item from entering the check-collection system or assume the risk of sending it forward.

Furthermore, the Board does not expect the amendments that remove references to cash and other specified forms of settlement to burden small entities, as the use of cash as settlement is rare and typically only done in emergency situations. The Board's final rule will allow use of cash as settlement in emergency situations by continuing to permit other forms of settlement to which the Reserve Banks agree. The Board does not expect the rule to have a significant economic impact on a substantial number of small entities.

List of Subjects in 12 CFR Part 210

Banks, Banking, Federal Reserve System.

Authority and Issuance

For the reasons set forth in the preamble, the Board amends 12 CFR part 210 as follows:

PART 210—COLLECTION OF CHECKS AND OTHER ITEMS BY FEDERAL RESERVE BANKS AND FUNDS TRANSFERS THROUGH FEDWIRE (REGULATION J)

1. The authority citation for part 210 continues to read as follows:

AUTHORITY: 12 U.S.C. 248 (i), (j), and (o); 12 U.S.C. 342; 12 U.S.C. 360; 12 U.S.C. 464; 12 U.S.C. 4001-4010; 12 U.S.C. 5001-5018.

2. In part 210, revise all references to "article 4A" to read "Article 4A."

Subpart A—Collection of Checks and Other Items by Federal Reserve Banks

3. In § 210.2, revise paragraphs (h), (i), (m), (n), (q), and (s)(1) to read as follows:

§210.2 Definitions.

* * * * *

(h) *Check* means a check or an electronic check, as those terms are defined in § 229.2 of this chapter (Regulation CC).

(i) *Item*. (1) Means—

(i) An instrument or a promise or order to pay money, whether negotiable or not, that is—

(A) Payable in a Federal Reserve District¹ (District);

(B) Sent by a sender to a Reserve Bank for handling under this subpart;
and

(C) Collectible in funds acceptable to the Reserve Bank of the District
in which the instrument is payable; or

(ii) A check.

(2) Unless otherwise indicated, *item* includes both a cash and a noncash item, and includes a returned check sent by a paying or returning bank. *Item* does not include a check that cannot be collected at par, or a *payment order* as defined in §210.26(i) and handled under subpart B of this part. The term also does not include an electronically-created item as defined in § 229.2 of this chapter (Regulation CC).

¹ For purposes of this subpart, the Virgin Islands and Puerto Rico are deemed to be in the Second District, and Guam, American Samoa, and the Northern Mariana Islands in the Twelfth District.

* * * * *

(m) *Returned check* means a cash item returned by a paying bank, including an electronic returned check as defined in § 229.2 of this chapter (Regulation CC) and a notice of nonpayment in lieu of a returned check, whether or not a Reserve Bank handled the check for collection.

(n) *Sender* means any of the following entities that sends an item to a Reserve Bank for forward collection—

(1) A *depository institution*, as defined in section 19(b) of the Federal Reserve Act (12 U.S.C. 461(b));

(2) A member bank, as defined in section 1 of the Federal Reserve Act (12 U.S.C. 221);

(3) A clearing institution, defined as—

(i) An institution that is not a depository institution but that maintains with a Reserve Bank the balance referred to in the first paragraph of section 13 of the Federal Reserve Act (12 U.S.C. 342); or

(ii) A corporation that maintains an account with a Reserve Bank in conformity with §211.4 of this chapter (Regulation K);

(4) Another Reserve Bank;

(5) An international organization for which a Reserve Bank is empowered to act as depository or fiscal agent and maintains an account;

(6) A foreign correspondent, defined as any of the following entities for which a Reserve Bank maintains an account: a foreign bank or banker, a foreign state as

defined in section 25(b) of the Federal Reserve Act (12 U.S.C. 632), or a foreign correspondent or agency referred to in section 14(e) of that act (12 U.S.C. 358); or

(7) A branch or agency of a foreign bank maintaining reserves under section 7 of the International Banking Act of 1978 (12 U.S.C. 347d, 3105).

* * * * *

(q) *Fedwire Funds Service* and *Fedwire* have the same meaning as that set forth in § 210.26(e).

* * * * *

(s) * * *

(1) The terms not defined herein have the meanings set forth in § 229.2 of this chapter applicable to subpart C or D of part 229 of this chapter (Regulation CC), as appropriate; and

* * * * *

4. In § 210.3, revise paragraph (a) to read as follows:

§210.3 General provisions.

(a) *General.* Each Reserve Bank shall receive and handle items in accordance with this subpart, and shall issue operating circulars governing the details of its handling of items and other matters deemed appropriate by the Reserve Bank. The circulars may, among other things, classify cash items and noncash items, require separate sorts and letters, provide different closing times for the receipt of different classes or types of items, provide for instructions by an Administrative Reserve Bank to other Reserve Banks, set forth terms of services, and establish procedures for adjustments on a Reserve Bank's books, including amounts, waiver of expenses, and payment of compensation. As deemed appropriate by the Reserve Bank, the circulars may also require the sender to provide warranties and indemnities

that only items and any noncash items the Reserve Banks have agreed to handle will be sent to the Reserve Banks. The Reserve Banks may provide to a subsequent collecting bank and to the paying bank any warranties and indemnities provided by the sender pursuant to this paragraph (a).

* * * * *

5. In § 210.4, revise paragraphs (a), (b)(1)(ii) and (iii), and (b)(3) to read as follows:

§210.4 Sending items to Reserve Banks.

(a) *Sending of items.* A sender's Administrative Reserve Bank may direct a sender other than a Reserve Bank to send any item to a specified Reserve Bank, whether or not the item is payable in the Reserve Bank's district.

(b) * * *

(1) * * *

(ii) The initial sender's Administrative Reserve Bank (which is deemed to have accepted deposit of the item from the initial sender);

(iii) The Reserve Bank that receives the item from the initial sender (if different from the initial sender's Administrative Reserve Bank); and

* * * * *

(3) The identity and order of the parties under paragraph (b)(1) of this section determine the relationships and the rights and liabilities of the parties under this subpart, part 229 of this chapter (Regulation CC), section 13(1) and section 16(13) of the Federal Reserve Act, and the Uniform Commercial Code. An initial sender's Administrative Reserve Bank that is deemed to accept an item for deposit or handle an item is also deemed to be a sender with respect to that item. The Reserve Banks that

are deemed to handle an item are deemed to be agents or subagents of the owner of the item, as provided in § 210.6(a).

* * * * *

6. In § 210.5, revise paragraphs (a), (c), (d), and (e) to read as follows:

§210.5 Sender's agreement; recovery by Reserve Bank.

(a) *Sender's agreement.* The warranties, indemnities, authorizations, and agreements made pursuant to this paragraph (a) may not be disclaimed and are made whether or not the item bears an indorsement of the sender. By sending an item to a Reserve Bank, the sender does all of the following.

(1) *Authorization to handle item.* The sender authorizes the sender's Administrative Reserve Bank and any other Reserve Bank or collecting bank to which the item is sent to handle the item (and authorizes any Reserve Bank that handles settlement for the item to make accounting entries), subject to this subpart and to the Reserve Banks' operating circulars, and warrants its authority to give this authorization.

(2) *Warranties for all items.* The sender warrants to each Reserve Bank handling the item that—

(i) The sender is a person entitled to enforce the item or authorized to obtain payment of the item on behalf of a person entitled to enforce the item;

(ii) The item has not been altered; and

(iii) The item bears all indorsements applied by parties that previously handled the item for forward collection or return.

(3) *Warranties and indemnities as set forth in Regulation CC and U.C.C.* As applicable and unless otherwise provided, the sender of an item makes to each Reserve

Bank that handles the item all the warranties and indemnities set forth in and subject to the terms of subparts C and D of part 229 of this chapter (Regulation CC) and Article 4 of the U.C.C. The sender makes all the warranties set forth in and subject to the terms of 4-207 of the U.C.C. for an electronic check as if it were an item subject to the U.C.C.

(4) *Warranties and indemnities as set forth in Reserve Bank operating circulars.* The sender makes any warranties and indemnities regarding the sending of items as set forth in an operating circular issued in accordance with § 210.3(a).

(5) *Sender's liability to Reserve Bank.* (i) Except as provided in paragraphs (a)(5)(ii) and (iii) of this section, the sender agrees to indemnify each Reserve Bank for any loss or expense sustained (including attorneys' fees and expenses of litigation) resulting from—

(A) The sender's lack of authority to make the warranty in paragraph

(a)(1) of this section;

(B) Any action taken by the Reserve Bank within the scope of its authority in handling the item; or

(C) Any warranty or indemnity made by the Reserve Bank under § 210.6(b), part 229 of this chapter, the U.C.C., or, regarding the sending of items, an operating circular issued in accordance with § 210.3(a).

(ii) A sender's liability for warranties and indemnities that the Reserve Bank makes for a substitute check, a paper or electronic representation thereof, or for an electronic check is subject to the following conditions and limitations—

(A) A sender of an original check shall not be liable under paragraph (a)(5)(i) of this section for any amount that the Reserve Bank pays under subpart D of part 229 of this chapter, or under § 229.34 of this chapter with respect to an electronic check, absent the sender's agreement to the contrary; and

(B) Nothing in this subpart alters the liability of a sender of a substitute check or paper or electronic representation of a substitute check under subpart D of part 229 of this chapter, or a sender of an electronic check under § 229.34 of this chapter.

(iii) A sender shall not be liable for any amount that the Reserve Bank pays under this subpart or part 229 of this chapter that is attributable to the Reserve Bank's own lack of good faith or failure to exercise ordinary care.

* * * * *

(c) *Recovery by Reserve Bank.* (1) A Reserve Bank that has handled an item may recover as provided in paragraph (c)(2) of this section if an action or proceeding is brought against (or if defense is tendered to) the Reserve Bank based on—

- (i) The alleged failure of the sender to have the authority to make the warranty and agreement in paragraph (a)(1) of this section;
- (ii) Any action by the Reserve Bank within the scope of its authority in handling the item; or
- (iii) Any warranty or indemnity made by the Reserve Bank under § 210.6(b), part 229 of this chapter, or the U.C.C.

(2) Upon entry of a final judgment or decree in an action or proceeding described in

paragraph (c)(1) of this section, a Reserve Bank may recover from the sender the amount of attorneys' fees and other expenses of litigation incurred, as well as any amount the Reserve Bank is required to pay because of the judgment or decree or the tender of defense, together with interest thereon.

(d) *Methods of recovery.* (1) The Reserve Bank may recover the amount stated in paragraph (c) of this section by charging any account on its books that is maintained or used by the sender (or by charging a Reserve Bank sender), if—

- (i) The Reserve Bank made seasonable written demand on the sender to assume defense of the action or proceeding; and
- (ii) The sender has not made any other arrangement for payment that is acceptable to the Reserve Bank.

(2) The Reserve Bank is not responsible for defending the action or proceeding before using this method of recovery. A Reserve Bank that has been charged under this paragraph (d) may recover from its sender in the manner and under the circumstances set forth in this paragraph (d).

(3) A Reserve Bank's failure to avail itself of the remedy provided in this paragraph (d) does not prejudice its enforcement in any other manner of the indemnity agreement referred to in paragraph (a)(5) of this section.

(e) *Security interest.* When a sender sends an item to a Reserve Bank, the sender and any prior collecting bank grant to the sender's Administrative Reserve Bank a security interest in all of their respective assets in the possession of, or held for the account of, any Reserve Bank to secure their respective obligations due or to become due to the Administrative Reserve Bank under this subpart or subpart C or D of part 229 of this chapter (Regulation CC). The

security interest attaches when a warranty is breached or any other obligation to the Reserve Bank is incurred. If the Reserve Bank, in its sole discretion, deems itself insecure and gives notice thereof to the sender or prior collecting bank, or if the sender or prior collecting bank suspends payments or is closed, the Reserve Bank may take any action authorized by law to recover the amount of an obligation, including, but not limited to, the exercise of rights of set off, the realization on any available collateral, and any other rights it may have as a creditor under applicable law.

7. In § 210.6:

- a. Remove the word “and” at the end of paragraph (a)(2)(ii).
- b. Revise paragraph (a)(2)(iii).
- c. Add paragraph (a)(2)(iv).
- d. Revise paragraphs (b) and (c).
- e. Remove paragraph (d).

The revisions and addition read as follows:

§210.6 Status, warranties, and liability of Reserve Bank.

(a) * * *

(2) * * *

(iii) As provided in an operating circular issued in accordance with § 210.3(a) regarding the sending of items; and

(iv) As provided in subparts C and D of part 229 of this chapter (Regulation CC).

* * * * *

(b) *Warranties and liability.* The following provisions apply when a Reserve Bank presents or sends an item.

(1) *Warranties for all items.* The Reserve Bank warrants to a subsequent collecting bank and to the paying bank and any other payor that—

(i) The Reserve Bank is a person entitled to enforce the item (or is authorized to obtain payment of the item on behalf of a person that is either entitled to enforce the item or authorized to obtain payment on behalf of a person entitled to enforce the item);

(ii) The item has not been altered; and

(iii) The item bears all indorsements applied by parties that previously handled the item for forward collection or return.

(2) *Warranties and indemnities as set forth in Reserve Bank operating circulars.* The Reserve Bank makes any warranties and indemnities regarding the sending of items as set forth in an operating circular issued in accordance with § 210.3(a).

(3) *Warranties and indemnities as set forth in Regulation CC and U.C.C.* As applicable and unless otherwise provided, the Reserve Bank makes all the warranties and indemnities set forth in and subject to the terms of subparts C and D of part 229 of this chapter (Regulation CC) and Article 4 of the U.C.C. The Reserve Bank makes all the warranties set forth in and subject to the terms of 4-207 of the U.C.C. for an electronic check as if it were an item subject to the U.C.C.

(4) *Indemnity for substitute check created from an electronic check.* (i) Except as provided in paragraph (b)(4)(ii) of this section, the Reserve Bank shall indemnify the bank to which it transfers or presents an electronic check (the recipient bank) for the

amount of any losses that the recipient bank incurs under subpart D of part 229 of this chapter (Regulation CC) for an indemnity that the recipient bank was required to make under subpart D of part 229 of this chapter in connection with a substitute check later created from the electronic check.

(ii) The Reserve Bank shall not be liable under paragraph (b)(4)(i) of this section for any amount that the recipient bank pays under subpart D of part 229 of this chapter that is attributable to the lack of good faith or failure to exercise ordinary care of the recipient bank or a person that handled the item, in any form, after the recipient bank.

(c) *Time for commencing action against Reserve Bank.* (1) A claim against a Reserve Bank for lack of good faith or failure to exercise ordinary care shall be barred unless the action on the claim is commenced within two years after the claim accrues. Such a claim accrues on the date when a Reserve Bank's alleged failure to exercise ordinary care or to act in good faith first results in damages to the claimant.

(2) A claim that arises under paragraph (b)(3) of this section shall be barred unless the action on the claim is commenced within one year after the claim accrues. Such a claim accrues as of the date on which the claimant first learns, or by which the claimant reasonably should have learned, of the facts and circumstances giving rise to the claim.

(3) This paragraph (c) does not alter the time limit for claims under § 229.38(g) of this chapter (which include claims for breach of warranty under § 229.34 of this chapter) or subpart D of part 229 of this chapter.

8. In § 210.7, revise paragraphs (a)(1) and (b)(2) to read as follows:

§210.7 Presenting items for payment.

(a) * * *

(1) A Reserve Bank or a subsequent collecting bank may present an item for payment or send the item for presentment and payment; and

* * *

(b) * * *

(2) In accordance with § 229.36 of this chapter (Regulation CC);

* * *

9. In § 210.9, revise paragraphs (b)(2)(i), (b)(3)(i)(A) and (B), (b)(4) through (6), and (c) through (e) and remove paragraph (f) to read as follows:

§210.9 Settlement and payment.

* * *

(b) * * *

(2) * * *

(i) On the day a paying bank receives a cash item from a Reserve Bank, it shall settle for the item so that the proceeds of the settlement are available to its Administrative Reserve Bank, or return the item, by the latest of—

(A) The next clock hour or clock half-hour that is at least one half-hour after the paying bank receives the item;

(B) 8:30 a.m. eastern time; or

(C) Such later time as provided in the Reserve Banks' operating circulars.

* * *

(3) * * *

(i) * * *

(A) On that day, settle for the item so that the proceeds of the settlement are available to its Administrative Reserve Bank, or return the item, by the latest of the next clock hour or clock half-hour that is at least one half-hour after it ordinarily would have received the item, 8:30 a.m. eastern time, or such later time as provided in the Reserve Banks' operating circulars; or

(B) On the next day that is a banking day for both the paying bank and the Reserve Bank, settle for the item so that the proceeds of the settlement are available to its Administrative Reserve Bank by 8:30 a.m. eastern time on that day or such later time as provided in the Reserve Banks' operating circulars; and compensate the Reserve Bank for the value of the float associated with the item in accordance with procedures provided in the Reserve Bank's operating circular.

* * * * *

(4) *Reserve Bank closed.* If a paying bank receives a cash item from a Reserve Bank on a banking day that is not a banking day for the Reserve Bank, the paying bank shall—

(i) Settle for the item so that the proceeds of the settlement are available to its Administrative Reserve Bank by the close of the Fedwire Funds Service on the Reserve Bank's next banking day, or return the item by midnight of the day it receives the item (if the paying bank fails to settle for or return a cash item in accordance with this paragraph (b)(4)(i), it shall become accountable for the

amount of the item as of the close of its banking day on the day it receives the item); and

(ii) Settle for the item so that the proceeds of the settlement are available to its Administrative Reserve Bank by 8:30 a.m. eastern time on the Reserve Bank's next banking day or such later time as provided in the Reserve Bank's operating circular, or return the item by midnight of the day it receives the item. If the paying bank fails to settle for or return a cash item in accordance with this paragraph (b)(4)(ii), it shall be subject to any applicable overdraft charges. Settlement under this paragraph (b)(4)(ii) satisfies the settlement requirements of paragraph (b)(4)(i) of this section.

(5) *Manner of settlement.* Settlement with a Reserve Bank under paragraphs (b)(1) through (4) of this section shall be made by debit to an account on the Reserve Bank's books or other form of settlement to which the Reserve Bank agrees, except that the Reserve Bank may, in its discretion, obtain settlement by charging the paying bank's account. A paying bank may not set off against the amount of a settlement under this section the amount of a claim with respect to another cash item, cash letter, or other claim under § 229.34 of this chapter (Regulation CC) or other law.

(6) *Notice in lieu of return.* If a cash item is unavailable for return, the paying bank may send a notice in lieu of return as provided in §229.31(f) of this chapter (Regulation CC).

(c) *Noncash items.* A Reserve Bank may require the paying or collecting bank to which it has presented or sent a noncash item to pay for the item by a debit to an account maintained or used by the paying or collecting bank on the Reserve Bank's books or by any other form of settlement acceptable to the Reserve Bank.

(d) *Nonbank payor.* A Reserve Bank may require a nonbank payor to which it has presented an item to pay for it by debit to an account on the Reserve Bank's books or other form of settlement acceptable to the Reserve Bank.

(e) *Liability of Reserve Bank.* Except as set forth in § 229.35(b) of this chapter (Regulation CC), a Reserve Bank shall not be liable for the failure of a collecting bank, paying bank, or nonbank payor to pay for an item, or for any loss resulting from the Reserve Bank's acceptance of any form of payment other than cash authorized in paragraphs (b), (c), and (d) of this section. A Reserve Bank that acts in good faith and exercises ordinary care shall not be liable for the nonpayment of, or failure to realize upon, any non-cash form of payment that it accepts under paragraphs (b), (c), and (d) of this section.

10. In § 210.10, revise paragraph (a) to read as follows:

§210.10 Time schedule and availability of credits for cash items and returned checks.

(a) Each Reserve Bank shall publish a time schedule indicating when the amount of any cash item or returned check received by it is counted toward the balance maintained to satisfy a reserve balance requirement for purposes of part 204 of this chapter (Regulation D) and becomes available for use by the sender or paying or returning bank. The Reserve Bank that holds the settlement account shall give either immediate or deferred credit to a sender, a paying bank, or a returning bank (other than a foreign correspondent) in accordance with the time schedule of the receiving Reserve Bank. A Reserve Bank ordinarily gives credit to a foreign correspondent only when the Reserve Bank receives payment of the item in actually and finally collected funds, but, in its discretion, a Reserve Bank may give immediate or deferred credit in accordance with its time schedule.

* * * * *

11. In § 210.11, revise paragraph (b) and remove paragraph (c) to read as follows:

§210.11 Availability of proceeds of noncash items; time schedule.

* * * * *

(b) *Time schedule.* A Reserve Bank may give credit for the proceeds of a noncash item subject to payment in actually and finally collected funds in accordance with a published time schedule. The time schedule shall indicate when the proceeds of the noncash item will be counted toward the balance maintained to satisfy a reserve balance requirement for purposes of part 204 of this chapter (Regulation D) and become available for use by the sender. A Reserve Bank may, however, refuse at any time to permit the use of credit given by it for a noncash item for which the Reserve Bank has not yet received payment in actually and finally collected funds.

12. In § 210.12, revise paragraphs (a) and (c) through (g) to read as follows:

§210.12 Return of cash items and handling of returned checks.

(a) *Return of items—(1) Return of cash items handled by Reserve Banks.* A paying bank that receives a cash item from a Reserve Bank, other than for immediate payment over the counter, and that settles for the item as provided in § 210.9(b), may, before it has finally paid the item, return the item to any Reserve Bank (unless its Administrative Reserve Bank directs it to return the item to a specific Reserve Bank) in accordance with subpart C of part 229 of this chapter (Regulation CC), the Uniform Commercial Code, and the Reserve Banks' operating circulars. A paying bank that receives a cash item from a Reserve Bank also may return the item prior to settlement, in accordance with § 210.9(b) and the Reserve Banks' operating circulars. The rules or practices of a clearinghouse through which the item was presented, or a special collection agreement under which the item was presented, may not extend these return times, but may provide for a shorter return time.

(2) *Return of checks not handled by Reserve Banks.* A paying bank that receives a check, other than from a Reserve Bank, and that determines not to pay the check, may send the returned check to any Reserve Bank (unless its Administrative Reserve Bank directs it to send the returned check to a specific Reserve Bank) in accordance with subpart C of part 229 of this chapter (Regulation CC), the Uniform Commercial Code, and the Reserve Banks' operating circulars. A returning bank may send a returned check to any Reserve Bank (unless its Administrative Reserve Bank directs it to send the returned check to a specific Reserve Bank) in accordance with subpart C of part 229 of this chapter (Regulation CC), the Uniform Commercial Code, and the Reserve Banks' operating circulars.

* * * * *

(c) *Paying bank's and returning bank's agreement.* The warranties, indemnities, authorizations, and agreements made pursuant to this paragraph (c) may not be disclaimed and are made whether or not the returned check bears an indorsement of the paying bank or returning bank. By sending a returned check to a Reserve Bank, the paying bank or returning bank does all of the following.

(1) *Authorization to handle returned check.* The paying bank or returning bank authorizes the paying bank's or returning bank's Administrative Reserve Bank, and any other Reserve Bank or returning bank to which the returned check is sent, to handle the returned check (and authorizes any Reserve Bank that handles settlement for the returned check to make accounting entries) subject to this subpart and to the Reserve Banks' operating circulars.

(2) *Warranties for all returned checks.* The paying bank or returning bank warrants to each Reserve Bank handling a returned check that the returned check bears all indorsements applied by parties that previously handled the returned check for forward collection or return.

(3) *Warranties and indemnities as set forth in Regulation CC.* As applicable and unless otherwise provided, a paying bank or returning bank makes to each Reserve Bank that handles the returned check all the warranties and indemnities set forth in and subject to the terms of subparts C and D of part 229 of this chapter (Regulation CC).

(4) *Paying bank or returning bank's liability to Reserve Bank.* (i) Except as provided in paragraph (c)(4)(ii) and (iii) of this section, a paying bank or returning bank agrees to indemnify each Reserve Bank for any loss or expense (including attorneys' fees and expenses of litigation) resulting from—

(A) The paying or returning bank's lack of authority to give the authorization in paragraph (c)(1) of this section;

(B) Any action taken by a Reserve Bank within the scope of its authority in handling the returned check; or

(C) Any warranty or indemnity made by the Reserve Bank under paragraph (e) of this section or part 229 of this chapter.

(ii) A paying bank's or returning bank's liability for warranties and indemnities that a Reserve Bank makes for a returned check that is a substitute check, a paper or electronic representation thereof, or an electronic returned check is subject to the following conditions and limitations—

(A) A paying bank or returning bank that sent an original returned check shall not be liable for any amount that a Reserve Bank pays under subpart D of part 229 of this chapter, or under § 229.34 of this chapter with respect to an electronic returned check, absent the paying bank's or returning bank's agreement to the contrary; and

(B) Nothing in this subpart alters the liability under subpart D of part 229 of this chapter of a paying bank or returning bank that sent a substitute check or a paper or electronic representation of a substitute check or under § 229.34 of this chapter of a paying bank or returning bank that sent an electronic returned check; and

(iii) A paying bank or returning bank shall not be liable for any amount that the Reserve Bank pays under this subpart or part 229 of this chapter that is attributable to the Reserve Bank's own lack of good faith or failure to exercise ordinary care.

(d) *Paying bank or returning bank's liability under other law.* Nothing in paragraph (c) of this section limits any warranty or indemnity by a returning bank or paying bank (or a person that handled an item prior to that bank) arising under state law or regulation (such as the U.C.C.), other federal law or regulation (such as part 229 of this chapter), or an agreement with a Reserve Bank.

(e) *Warranties by and liability of Reserve Bank--(1) Warranties and indemnities.* The following provisions apply when a Reserve Bank handles a returned check under this subpart.

(i) *Warranties for all items.* The Reserve Bank warrants to the bank to which it sends the returned check that the returned check bears all indorsements applied

by parties that previously handled the returned check for forward collection or return.

(ii) *Warranties and indemnities as set forth in Regulation CC.* As applicable and unless otherwise provided, the Reserve Bank makes all the warranties and indemnities set forth in and subject to the terms of subparts C and D of part 229 of this chapter (Regulation CC).

(2) *Indemnity for substitute check created from electronic returned check.* (i) Except as provided in paragraph (e)(2)(ii) of this section, the Reserve Bank shall indemnify the bank to which it transfers or presents an electronic returned check (the recipient bank) for the amount of any losses that the recipient bank incurs under subpart D of part 229 of this chapter (Regulation CC) for an indemnity that the recipient bank was required to make under subpart D of part 229 of this chapter in connection with a substitute check later created from the electronic returned check.

(ii) The Reserve Bank shall not be liable under paragraph (e)(2)(i) of this section for any amount that the recipient bank pays under subpart D of part 229 of this chapter that is attributable to the lack of good faith or failure to exercise ordinary care of the recipient bank or a person that handled the item, in any form, after the recipient bank.

(3) *Liability of Reserve Bank.* A Reserve Bank shall not have or assume any other liability to any person except—

- (i) For the Reserve Bank's own lack of good faith or failure to exercise ordinary care;
- (ii) As provided in this paragraph (e); and

(iii) As provided in subparts C and D of part 229 of this chapter (Regulation CC).

(f) *Recovery by Reserve Bank.* (1) A Reserve Bank that has handled a returned check may recover as provided in paragraph (f)(2) of this section if an action or proceeding is brought against (or if defense is tendered to) the Reserve Bank based on—

(i) The alleged failure of the paying bank or returning bank to have the authority to give the authorization in paragraph (c)(1) of this section;

(ii) Any action by the Reserve Bank within the scope of its authority in handling the returned check; or

(iii) Any warranty or indemnity made by the Reserve Bank under paragraph (e) of this section or part 229 of this chapter; and

(2) Upon entry of a final judgment or decree in an action or proceeding described in paragraph (f)(1) of this section, a Reserve Bank may recover from the paying bank or returning bank the amount of attorneys' fees and other expenses of litigation incurred, as well as any amount the Reserve Bank is required to pay because of the judgment or decree or the tender of defense, together with interest thereon.

(g) *Methods of recovery.* (1) The Reserve Bank may recover the amount stated in paragraph (f) of this section by charging any account on its books that is maintained or used by the paying bank or returning bank (or by charging another returning Reserve Bank), if—

(i) The Reserve Bank made seasonable written demand on the paying bank or returning bank to assume defense of the action or proceeding; and

(ii) The paying bank or returning bank has not made any other arrangement for payment that is acceptable to the Reserve Bank.

(2) The Reserve Bank is not responsible for defending the action or proceeding before using this method of recovery. A Reserve Bank that has been charged under this paragraph (g) may recover from the paying or returning bank in the manner and under the circumstances set forth in this paragraph (g).

(3) A Reserve Bank's failure to avail itself of the remedy provided in this paragraph (g) does not prejudice its enforcement in any other manner of the indemnity agreement referred to in paragraph (c)(4) of this section.

* * * * *

Subpart B—Funds Transfers Through Fedwire

13. In § 210.25:

- a. In paragraphs (a) and (b)(3), remove the word "Fedwire" and add in its place the words "the Fedwire Funds Service".
- b. Revise the introductory text of paragraph (b)(2).
- c. Add paragraph (e).

The revision and addition read as follows:

§210.25 Authority, purpose, and scope.

* * * * *

(b) * * *

(2) Except as otherwise provided in paragraphs (b)(3) and (4) of this section, including Article 4A as set forth in appendix B to this subpart, and operating circulars of the Reserve Banks issued in accordance with paragraph (c) of this section, this subpart governs the rights and obligations of:

* * * * *

(e) *Financial messaging standards*. Financial messaging standards (e.g., ISO 20022), including the financial messaging components, elements, technical documentation, tags, and terminology used to implement those standards, do not confer or connote legal status or responsibilities. This subpart, including Article 4A as set forth in appendix B to this subpart, and the operating circulars of the Reserve Banks issued in accordance with paragraph (c) of this section govern the rights and obligations of parties to funds transfers sent through the Fedwire Funds Service as provided in paragraph (b) of this section. To the extent there is any inconsistency between a financial messaging standard adopted by the Fedwire Funds Service and this subpart, this subpart shall prevail.

14. In § 210.26, revise paragraph (e) to read as follows:

§210.26 Definitions.

* * * * *

(e) *Fedwire Funds Service* and *Fedwire* means the funds-transfer system owned and operated by the Federal Reserve Banks that is used primarily for the transmission and settlement of payment orders governed by this subpart. Fedwire does not include the system for making automated clearing house transfers.

* * * * *

§210.29 [Amended]

15. In §210.29(b), remove the word “Fedwire” and add in its place the words “the Fedwire Funds Service”.

16. In appendix A to subpart B:

- a. Under “Section 210.25—Authority, Purpose, and Scope”, add paragraph (e).
- b. Under “Section 210.32—Federal Reserve Bank Liability; Payment of Interest”, revise paragraph (b).

The addition and revision read as follows:

Appendix A to Subpart B of Part 210—Commentary

* * * * *

Section 210.25—Authority, Purpose, and Scope

* * * * *

(e) *Financial messaging standards.* This paragraph makes clear that financial messaging standards, including the financial messaging components, elements, technical documentation, tags, and terminology used to implement those standards, do not confer or connote legal status or responsibilities. Instead, subpart B of this part and Federal Reserve Bank operating circulars govern the rights and obligations of parties to funds transfers sent through the Fedwire Funds Service as provided in § 210.25(b). Thus, to the extent there is any inconsistency between a financial messaging standard adopted by the Fedwire Funds Service and subpart B of this part, subpart B of this part, including Article 4A as adopted in appendix B to subpart B of this part, will prevail. In the ISO 20022 financial messaging standard, for example, the term *agent* is used to refer to a variety of bank parties to a funds transfer (e.g., *debtor agent*, *creditor agent*, *intermediary agent*). Notwithstanding use of that term in the standard and in message tags, such banks are not the agents of any party to a funds transfer and owe no duty to any other party to such a funds transfer except as provided in subpart B of

this part (including Article 4A) or by express agreement. The ISO 20022 financial messaging standard also permits information to be carried in a funds-transfer message regarding persons that are not parties to that funds transfer (e.g., *ultimate debtor*, *ultimate creditor*, *initiating party*) for regulatory, compliance, remittance, or other purposes. An “ultimate debtor” is not an “originator” as defined in Article 4A. The relationship between the ultimate debtor and the originator (what the ISO 20022 standard calls the “debtor”) is determined by law other than Article 4A.

* * * * *

Section 210.32—Federal Reserve Bank Liability; Payment of Interest

* * * * *

(b) *Payment of interest.* (1) Under article 4A, a Federal Reserve Bank may be required to pay compensation in the form of interest to another party in connection with its handling of a funds transfer. For example, payment of compensation in the form of interest is required in certain situations pursuant to sections 4A-204 (relating to refund of payment and duty of customer to report with respect to unauthorized payment order), 4A-209 (relating to acceptance of payment order), 4A-210 (relating to rejection of payment order), 4A-304 (relating to duty of sender to report erroneously executed payment order), 4A-305 (relating to liability for late or improper execution or failure to execute a payment order), 4A-402 (relating to obligation of sender to pay receiving bank), and 4A-404 (relating to obligation of beneficiary's bank to pay and give notice to beneficiary).

(2) Section 210.32(b) requires Federal Reserve Banks to provide compensation through an explicit interest payment. Under section 4A-506(a), the amount of such interest may be determined by agreement between the sender and receiving bank or by funds-transfer system

rule. If there is no such agreement, under section 4A-506(b), the amount of interest is based on the federal funds rate. Similarly, compensation in the form of explicit interest will be paid to government senders, receiving banks, or beneficiaries described in §210.25(d) if they are entitled to interest under this subpart. A Federal Reserve Bank may also, in its discretion, pay explicit interest directly to a remote party to a Fedwire funds transfer that is entitled to interest, rather than providing compensation to its direct sender or receiving bank.

(3) If a bank that received an explicit interest payment is not the party entitled to interest compensation under article 4A, the bank must pass the benefit of the explicit interest payment made to it to the party that is entitled to compensation in the form of interest from a Federal Reserve Bank. The benefit may be passed on either in the form of a direct payment of interest or in the form of a compensating balance, if the party entitled to interest agrees to accept the other form of compensation, and the value of the compensating balance is at least equivalent to the value of the explicit interest that otherwise would have been provided.

* * * * *

By order of the Board of Governors of the Federal Reserve System, November 14, 2018.

Ann Misback,

Secretary of the Board.

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